

COSTA MESA SANITARY DISTRICT

Financial Statements

Year ended June 30, 2001

(With Independent Auditors' Report Thereon)

COSTA MESA SANITARY DISTRICT

Financial Statements

Year ended June 30, 2001

(with comparative totals for the year ended June 30, 2000)

TABLE OF CONTENTS

	<u>Page</u>
Independent Auditors' Report	1
Financial Statements:	
Balance Sheet	2
Statement of Revenues, Expenses and Changes in Retained Earnings	3
Statement of Cash Flows	4
Notes to Financial Statements	6

COSTA MESA SANITARY DISTRICT

Balance Sheet

June 30, 2001

(with comparative totals as of June 30, 2000)

<u>Assets</u>	<u>2001</u>	<u>2000</u>
Current assets:		
Cash and investments (note 2)	\$ 10,080,554	9,849,400
Accounts receivable	7,899	3,443
Interest receivable	110,442	134,057
Taxes receivable	105,167	84,776
Due from other governments	<u>58,763</u>	<u>16,489</u>
Total current assets	<u>10,362,825</u>	<u>10,088,165</u>
Property, plant and equipment:		
Property rights	4,025	4,025
Subsurface sewer lines	19,782,467	19,305,508
Buildings and improvements	346,520	346,520
Equipment	458,725	450,355
Construction in progress	<u>192,905</u>	<u>365,264</u>
Total property, plant and equipment	20,784,642	20,471,672
Less accumulated depreciation	<u>(9,969,446)</u>	<u>(9,520,697)</u>
Net property, plant and equipment	<u>10,815,196</u>	<u>10,950,975</u>
Total assets	<u>\$ 21,178,021</u>	<u>21,039,140</u>
<u>Liabilities and District Equity</u>		
Current liabilities:		
Accounts payable	\$ 570,705	438,436
Deposits payable	-	72,298
Sales and use tax payable	400	-
Due to other governments	<u>-</u>	<u>225,481</u>
Total current liabilities	<u>571,105</u>	<u>736,215</u>
District equity:		
Contributed capital	<u>4,706,829</u>	<u>4,670,879</u>
Retained earnings:		
Investment in net property, plant and equipment	6,108,367	6,280,096
Reserved for capital outlay	3,650,922	3,231,303
Available for appropriation	<u>6,140,798</u>	<u>6,120,647</u>
Total retained earnings	<u>15,900,087</u>	<u>15,632,046</u>
Total district equity	<u>20,606,916</u>	<u>20,302,925</u>
Total liabilities and district equity	<u>\$ 21,178,021</u>	<u>21,039,140</u>

See accompanying notes to financial statements.

COSTA MESA SANITARY DISTRICT

Statement of Revenues, Expenses and Changes in Retained Earnings

Year ended June 30, 2001

(with comparative totals for the year ended June 30, 2000)

	<u>2001</u>	<u>2000</u>
Operating revenues:		
Trash assessments	\$ 3,676,200	3,242,526
Sewer assessments	1,508,150	1,382,405
Permits and inspection fees	21,445	26,089
Connection fees	67,763	108,121
Other services	91,017	39,771
Investment recovery	140,949	423,128
Excessive effluent discharge	<u>2,016</u>	<u>8,726</u>
Total operating revenues	<u>5,507,540</u>	<u>5,230,766</u>
Operating expenses:		
Solid waste disposal	2,758,872	2,071,705
Liquid waste disposal	508,388	500,839
Dump charges	1,666,619	1,638,937
General and administration	547,557	375,408
Depreciation	<u>448,748</u>	<u>413,113</u>
Total operating expenses	<u>5,930,184</u>	<u>5,000,002</u>
Operating income (loss)	<u>(422,644)</u>	<u>230,764</u>
Non-operating revenues (expenses):		
Investment income	670,091	426,803
Taxes	151,426	625,973
Annexation fees	-	86
Other revenues (expenses)	<u>(155,135)</u>	<u>(761)</u>
Total non-operating revenues (expenses)	<u>666,382</u>	<u>1,052,101</u>
Net income	243,738	1,282,865
Retained earnings at beginning of year, as restated (note 3)	<u>15,656,349</u>	<u>14,349,181</u>
Retained earnings at end of year	<u>\$ 15,900,087</u>	<u>15,632,046</u>

See accompanying notes to financial statements.

COSTA MESA SANITARY DISTRICT

Statement of Cash Flows

Year ended June 30, 2001

(with comparative totals for the year ended June 30, 2000)

	<u>2001</u>	<u>2000</u>
Cash flows from operating activities:		
Cash received from customers	\$ 5,460,810	5,383,671
Cash payments to suppliers for goods and services	<u>(5,084,928)</u>	<u>(4,055,604)</u>
Net cash provided by operating activities	<u>375,882</u>	<u>1,328,067</u>
Cash flows from non-capital financing activities:		
Taxes received	131,035	544,057
Annexation fees received	-	86
Miscellaneous cash payments	(155,235)	(761)
Miscellaneous cash revenue	<u>100</u>	<u>-</u>
Net cash provided by (used for) non-capital financing activities	<u>(24,100)</u>	<u>543,382</u>
Cash flows from capital and related financing activities:		
Cash paid to acquire fixed assets	<u>(814,334)</u>	<u>(462,493)</u>
Cash flows from investing activities:		
Purchase of investments	(2,000,000)	(3,978,872)
Proceeds from sale of investments	3,978,872	1,000,000
Interest received	<u>693,706</u>	<u>385,734</u>
Net cash provided by (used for) investing activities	<u>2,672,578</u>	<u>(2,593,138)</u>
Net increase (decrease) in cash and cash equivalents	2,210,026	(1,184,182)
Cash and cash equivalents at beginning of year	<u>5,870,528</u>	<u>7,054,710</u>
Cash and cash equivalents at end of year	<u>\$ 8,080,554</u>	<u>5,870,528</u>
Reconciliation of cash and cash equivalents to amounts reported on the balance sheet:		
Reported on the balance sheet:		
Cash and investments	\$ 10,080,554	9,849,400
Less investments not meeting the definition of cash equivalents:		
Federal Agency Securities	<u>(2,000,000)</u>	<u>(3,978,872)</u>
Cash and cash equivalents at end of year	<u>\$ 8,080,554</u>	<u>5,870,528</u>

(continued)

COSTA MESA SANITARY DISTRICT

Statement of Cash Flows

(Continued)

	<u>2001</u>	<u>2000</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income (loss)	\$ (422,644)	<u>230,764</u>
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	448,748	413,113
Disposal of fixed assets	537,315	173,705
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	(4,456)	30,251
(Increase) decrease in trash assessments receivable	-	60,843
(Increase) decrease in sewer assessments receivable	-	29,064
(Increase) decrease in due from other governments	(42,274)	32,747
(Increase) decrease in prepaid insurance	-	35,738
Increase (decrease) in accounts payable	156,572	96,731
Increase (decrease) in due to City of Costa Mesa	(225,481)	225,481
Increase (decrease) in deposits payable	(72,298)	-
Increase (decrease) in sales and use tax payable	<u>400</u>	<u>(370)</u>
Total adjustments	<u>798,526</u>	<u>1,097,303</u>
Net cash provided by operating activities	<u>\$ 375,882</u>	<u>1,328,067</u>

Non-cash investing, capital, and financing activities

During the years ended June 30, 2001 and June 30, 2000, assets of \$35,950 and \$6,675 were contributed to the District by developers, respectively.

See accompanying notes to financial statements.

COSTA MESA SANITARY DISTRICT

Notes to Financial Statements

Year ended June 30, 2001

(1) Summary of Significant Accounting Policies

The Costa Mesa Sanitary District ("District") was incorporated in February 1944 pursuant to Division VI, Part 1 of the Health and Safety Code of the State of California (sometimes referred to as the Sanitary District Act of 1923). At the present time, the boundaries of the District extend into the Cities of Costa Mesa and Newport Beach as well as unincorporated areas within the County of Orange.

On December 19, 1955, the District entered into an agreement with the City of Costa Mesa, pursuant to the authority contained in the Joint Exercise of Powers Act (Sections 6500-6513 of the Government Code). Currently, the City has been contracted by the District to provide maintenance services related to the sewer system.

The following is a summary of the District's significant accounting policies:

(a) Basis of Accounting

The District uses the accrual basis of accounting. Revenues are recognized when they are earned and expenses are recorded when the liability is incurred for receipt of the related goods and services.

(b) Investments

Investments are reported in the accompanying balance sheet at fair value. Changes in fair value that occur during a fiscal year are recognized as *investment income* reported for that fiscal year. *Investment income* includes interest earnings, changes in fair value, and any gains or losses realized upon the liquidation, maturity, or sale of investments.

(c) Cash Equivalents

For purposes of the statement of cash flows, cash equivalents are defined as short-term, highly liquid investments that are both readily convertible to known amounts of cash or so near their maturity that they present insignificant risk of changes in value because of changes in interest rates, and have an original maturity date of three months or less. Investments in federal agency securities are not considered to be cash equivalents as defined above and, therefore, are excluded from the statements of cash flows.

(d) Fixed Assets

Fixed assets purchased by the District are capitalized at historical cost. Data reflected in the District fixed asset records include estimates of original cost as determined by knowledgeable District personnel. Contributed fixed assets,

consisting primarily of donated subsurface lines dedicated to the District by sub-

COSTA MESA SANITARY DISTRICT

Notes to Financial Statements

(Continued)

(1) Summary of Significant Accounting Policies, (Continued)

(d) Fixed Assets, (Continued)

dividers, are recorded as increases in the contributed capital of the District. Such contributed fixed assets are recorded at their fair market value at the time of donation. Depreciation is charged to operations using the straight-line method based on the estimated useful life of the asset. The estimated useful lives are as follows:

Buildings	20 years
Improvements	20 years
Equipment	20 years
Subsurface sewer lines	60 years

(2) Cash and Investments

Cash and investments held by the Sanitary District at June 30, 2001 consisted of the following:

Deposits	\$ (136,620)
Investments	<u>10,217,174</u>
Total cash and investments	<u>\$10,080,554</u>

The Costa Mesa Sanitary District is generally authorized under the state statute and local resolutions to invest in U.S. Treasury bills, U.S. Treasury notes, Federal agency securities, banker's acceptances, certificates of deposit, negotiable certificates of deposit, commercial paper, medium term notes, repurchase agreements, Local Agency Investment Fund of the State of California, Orange County Treasurer's Pool, asset-backed and mortgage-backed securities, money market mutual funds, and passbook savings account demand deposits.

The District has also established guidelines for security purchases with investment limitations as follows: Bankers acceptances may not exceed 40% of the District's surplus money. Negotiable certificates of deposits may not exceed 30% of the District's surplus money. Commercial paper may not exceed 180 days maturity nor exceed 30% of the District's surplus funds. Medium term corporate notes may not exceed 30% of the District's surplus funds. The District may not invest more than 10% of its surplus funds in reverse repurchase agreements, and must always match its maturities to the reinvestment. The District may not invest more than 35% of its surplus money with the Orange County Treasurer's Pool. Asset-backed and mortgage-backed securities may not exceed 20% of the District's surplus money.

COSTA MESA SANITARY DISTRICT

Notes to Financial Statements

(Continued)

(2) Cash and Investments, (Continued)

Under the California Government Code, a financial institution is required to secure deposits made by state or local governmental units by pledging securities held in the form of an undivided collateral pool. The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure District deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

Deposits of cities and other state or local governments are classified in three categories to give an indication of the level of custodial risk assumed by the entity at year end. Category 1 includes deposits that are insured or collateralized with securities held by the District or its agent in the District's name. Category 2 includes deposits collateralized with securities held by the pledging financial institution's trust department or agent in the District's name. Category 2 also includes deposits collateralized by an interest in an undivided collateral pool held by an authorized agent of depository and subject to certain regulatory requirements under State law. Category 3 includes deposits collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the District's name. Category 3 also includes any uncollateralized deposits.

<u>Form of Deposit</u>	<u>Category</u>			<u>Bank Balance</u>	<u>Carrying Amount</u>
	<u>1</u>	<u>2</u>	<u>3</u>		
Demand deposits	<u>\$73,763</u>	<u>-</u>	<u>-</u>	<u>73,763</u>	<u>(136,620)</u>

Investments of cities and other state or local governments are classified in three categories to give an indication of the level of custodial risk assumed by the entity at year end. Category 1 includes investments that are insured, registered or are held by the District or its agent (other than the institution through which the District purchased the securities) in the District's name. Investments held "in the District's name" include securities held in a separate custodial or fiduciary account and identified as owned by the District in the custodian's internal accounting records. Category 2 includes uninsured and unregistered securities which are held in the District's name by the counterparty's trust department or agent. Category 3 includes uninsured and unregistered securities which are held by the counterparty, or the counterparty's trust department or agent, but not in the District's name. The counterparty is the party that acts as the broker-dealer agent of the District (the party that purchased the securities on behalf of the District). Category 3 includes all securities held by the broker-dealer of the District, regardless of whether or not the securities are being held in the District's name:

COSTA MESA SANITARY DISTRICT

Notes to Financial Statements

(Continued)

(2) Cash and Investments, (Continued)

	<u>Category</u>			<u>Carrying</u>
	<u>1</u>	<u>2</u>	<u>3</u>	<u>Amount</u>
Investments held by the District:				
Medium term corporate notes	\$2,472,114	-	-	2,472,114
Federal Agency Securities	<u>2,000,000</u>	<u>-</u>	<u>-</u>	2,000,000
	<u>\$4,472,114</u>	<u>-</u>	<u>-</u>	
Investments held by District not subject to categorization:				
Investment in State Investment Pool - LAIF				<u>5,745,060</u>
Total investments				<u>\$10,217,174</u>

The District is a voluntary participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. The fair value of the District's investment in this pool is reported in the accompanying financial statements at amounts based upon the District's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis. Included in LAIF's investment portfolio are collateralized mortgage obligations, mortgage-backed securities, other asset-backed securities, loans to certain state funds, and floating rate securities issued by federal agencies, government-sponsored enterprises, and corporations.

(3) Restatement of Beginning Retained Earnings

The accompanying financial statements reflect adjustments which resulted in a restatement of beginning retained earnings. The following schedule summarizes the effects of the prior period adjustment on the beginning retained earnings as of June 30, 2000:

Retained earnings at beginning of year, as previously reported	\$15,632,046
Adjustment of retained earnings:	
Adjustment of accounts payable	<u>24,303</u>
Retained earnings at beginning of year, as restated	<u>\$15,656,349</u>

COSTA MESA SANITARY DISTRICT

Notes to Financial Statements

(Continued)

(4) Subsequent Events

On July 12, 2001, the Costa Mesa Sanitary District entered into a 10 year lease agreement with the Municipal Finance Corporation to provide financing in the amount of \$2,200,000 for the acquisition of refuse containers. The lease provides a purchase option. The obligation is due in semi-annual principal and interest payments of \$140,591. Interest is computed at a stated rate of 4.92%.